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In the Supreme Court of the United States

OCTOBER TERM, 1928

No. 46

THE UNITED STATES, PETITIONER

v.

THE CAMBRIDGE LOAN AND BUILDING COMPANY

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

MOTION TO REMAND

Comes now the United States, the petitioner herein, by the Solicitor General, and moves the Court to remand the above entitled cause to the Court of Claims for additional Findings of Fact as hereinafter set forth.

Your petitioner shows to the Court that this case presents the question whether respondent is entitled to exemption as a building and loan association from income taxes under the Revenue Acts of 1918 and 1921. Taxes for the years 1918 to 1923, inclusive, are involved. The years 1918, 1919, and 1920 are controlled by the Revenue Act of 1918. Under Section 231 (4) of said Act (c. 18, 40 Stat. 1057,

1076) exemption is granted to "domestic building and loan associations and cooperative banks without capital stock organized and operated for mutual purposes and without profit." The taxes for the years 1921, 1922, and 1923 are controlled by Section 231 (4) of the Revenue Act of 1921 (c. 136, 42 Stat. 227, 253) which provides that exemption should be granted to "domestic building and loan associations substantially all the business of which is confined to making loans to members."

The Court of Claims made certain Findings of Fact (R. 8-11) and concluded that the respondent was not liable for the taxes in question, and thereupon rendered a judgment against the Government in favor of said respondent for the recovery of the taxes so paid, the substance and effect of the holding of the Court of Claims being that under either Act a building and loan association, recognized as such by the laws of the State under which it exists, is entitled to exemption from such Federal taxes merely because it is defined as a building and loan association by the State laws. The Government contends that under both Acts a building and loan association, to be entitled to exemption, must conduct its business as a building and loan association in fact and not merely be designated as such under the laws of the State of its origin.

The Government contends that, upon the facts found by the Court of Claims, the judgment of said court is erroneous and should be reversed. The

Government further contends that there are additional facts, fully supported by the evidence before the Court of Claims, which are material to a proper determination of the questions presented; that it requested Findings of Fact upon said matters which the Court of Claims failed and refused to make; that it renewed its request for such findings by a motion for a new trial, which the Court of Claims overruled and again failed and refused to make such findings. The Government represents to the Court that the following facts and each of them are relevant and material and have an important bearing upon the proper determination of the question involved in this case:

1. The dividends paid on running stock, i. e., stock subscribed for to be paid for in installments, steadily decreased, while dividends on paid-up stock steadily increased.

2. Deposits were accepted in large amounts, regardless of the borrowing needs of members, for the purpose of realizing pecuniary profit by lending such deposits to nonmembers, including building and loan associations and other financial institutions, and by making investments in mortgages or other securities purchased from nonmembers.

3. The respondent was not concerned with the purpose of the borrower and did not limit its loans to those to be used for building or otherwise acquiring homes. It accepted as security for members' and nonmembers' loans mortgages on homes, real

estate, farms, business properties, churches, and apartment houses, as well as bank stock, industrial stock, municipal and other bonds.

4. Respondent's loans to members were not confined to borrowers who subscribed to stock equal to the face of the loan, but it permitted persons to become members upon subscribing to a nominal amount of stock (from one to five shares), regardless of the amount sought to be borrowed. Retroactive nominal stock subscriptions were received by respondent and, in certain cases, credits of the borrower were applied by respondent to nominal stock where no stock subscriptions had been made by the borrower.

5. The number of depositors in every year exceeded the number of stockholders, the difference being small in 1918, but thereafter being approximately twice as great in each year except 1923, when it was more than three times as great.

Wherefore, it is respectfully prayed that this Court enter an order remanding said case to the Court of Claims for findings upon each and every one of the facts above set forth and upon such further and additional facts, if any, as to this Court may seem necessary.

Respectfully submitted.

WILLIAM D. MITCHELL,
Solicitor General.

HERMAN J. GALLOWAY,
Assistant Attorney General.

BRIEF ON MOTION TO REMAND

This case involves the question whether respondent is entitled to exemption from income tax as a building and loan association under the Revenue Acts of 1918 and 1921. The years 1918 to 1923, both inclusive, are involved; the years 1918, 1919, and 1920 being governed by the Act of 1918 and the years 1921, 1922, and 1923, by the Act of 1921. The Court of Claims in substance has held that if an organization is recognized as a building and loan association under the laws of the State of its origin it is entitled to exemption from tax under the Revenue Acts. The theory of the Government is that in order to be entitled to such exemption the organization must be a building and loan association in fact and not merely in name.

The Government contends that the purposes, characteristics, and method of operation of building and loan associations in the true sense are generally known and recognized both by the lawyer and the layman. Those purposes are the raising by subscriptions of the members of a fund for making advances to members to enable them to build or buy homes. The capital funds of such associations are derived from periodical payments by members, interest and premiums paid by borrowing members,

fixed periodical installments by borrowing members, fines, forfeitures, entrance fees and fees of a similar nature, all of which go into the common treasury; and when the installment payments and profits equal the face value of the shares issued, the shares are said to mature and the face value thereof is distributed to the stockholders owning the same.

A member is entitled to borrow, on sufficient mortgage security, an amount equal to his subscription for shares, and when his shares are paid up they operate to cancel his indebtedness. Such associations are distinctly and fundamentally not money-making enterprises but are essentially mutual and cooperative. The membership consists of borrowers and lenders and the profits inure equally to such members. These associations serve a unique public purpose. They encourage thrift. They enable persons who might otherwise be unable to own their homes to become independent in that respect. And it is because of the mutual and more or less altruistic purposes that such associations have been relieved of some of the burdens imposed upon companies or organizations engaged in business for a profit.

It is the Government's theory that these things were what Congress had in mind in granting exemption from income tax liabilities to building and loan associations, and that whenever it becomes apparent that an organization has departed from the fundamental purposes, characteristics and methods

of operation of such an association, it ceases to be within the spirit, purpose, or express provisions of such exemption.

With this theory in mind, the Government urged in the Court of Claims facts which it contended show a departure by respondent in these respects. The Court of Claims made findings of fact and upon those findings of fact the Government believes the decision of that court is erroneous and must be reversed. But there were other facts which the Government feels are material and proper for consideration and determination of the questions involved. The Court of Claims failed and refused to make such findings of fact, and though the questions were again presented upon the motion for new trial, that Court again failed and refused to make findings thereon.

Each of the matters referred to in the motion to remand will now be discussed separately.

I

THE DIVIDENDS PAID ON RUNNING STOCK, I. E., STOCK SUBSCRIBED FOR TO BE PAID IN INSTALLMENTS, STEADILY DECREASED, WHILE DIVIDENDS ON PAID-UP STOCK STEADILY INCREASED

Findings of fact upon such question would have an important bearing as showing that the business was being run primarily as a money-making enterprise and for the benefit of the paid-up stockholders thereof, thus materially departing from the

fundamental purpose of mutuality underlying true building and loan associations. In Request No. VIII for Findings of Fact in the Court of Claims the Government requested the Court of Claims to find as follows:

> Claimant, during the years 1918 to 1923, inclusive, paid dividends on running stock, paid-up stock, and loan stock; as follows:

Year	Per cent	On running stock	On paid-up stock	On loan stock
1918	5	$11,555.11	$2,525.72	$1,939.58
1919	5	11,267.16	3,440.16	1,946.59
1920	6	11,174.80	3,405.17	2,259.72
1921	7	12,906.71	6,578.82	2,826.33
1922	7	10,928.55	8,579.49	2,503.40
1923	7	9,396.78	12,080.09	1,842.96

These facts were set forth as Exhibit No. 7 of an agreed statement of facts and therefore are not in dispute. In the motion for new trial (pp. 10 and 11 of such motion) the Government renewed that request and stated that obviously, with its business rapidly increasing, respondent's dividends on running stock would likewise have been steadily increasing had respondent's business been conducted in the manner of a true building and loan association, i. e., by requiring borrowers to subscribe for running or installment stock equal to the loan made. It was set out in said motion for new trial (p. 11):

> The evidence shows that plaintiff had practically ceased to issue installment stock (R. pp. 50, 51), with the evident purpose and intention of increasing the profits of its pre-

paid stockholders, and this was accomplished by accepting nominal stock subscriptions of from one to five shares.

The evidence (R. p. 55) shows plaintiff's purpose:

670. Question. You mean that at the time of the making of the loans they were not members of the association, but subsequently made application for stock loans, retroactive loans?

Answer. That is what you would call it. And in addition to that——

671. Question. And for how much were these retroactive loans? That is, the number of shares?

Answer. They were——

672. Question. One?

Answer. One and two shares.

673. Question. One and two shares, nominal subscriptions to the stock?

Answer. Nominal subscriptions.

674. Question. And what was the purpose of that, sir?

Answer. To make them members.

675. Question. To make them members?

Answer. Yes, sir.

676. Question. Because you conceived that would reduce your tax liability?

Answer. Yes, sir.

II

DEPOSITS WERE ACCEPTED IN LARGE AMOUNTS, REGARDLESS OF THE BORROWING NEEDS OF MEMBERS, FOR THE PURPOSE OF REALIZING PECUNIARY PROFITS BY LENDING SUCH DEPOSITS TO NONMEMBERS, INCLUDING BUILDING AND LOAN ASSOCIATIONS AND OTHER FINANCIAL INSTITUTIONS, AND BY MAKING INVESTMENTS IN MORTGAGES OR OTHER SECURITIES PURCHASED FROM NONMEMBERS

While substantially this same conclusion can be drawn and inferred from a consideration of the figures and tables in the findings of fact made by the Court of Claims, the matter suggested and requested is an ultimate fact which has important bearing as showing a material departure by respondent from the methods of operation of a true building and loan association.

In Request No. II for Findings of Fact the Government asked the Court of Claims to find as follows:

> During the years 1918 to 1923, inclusive, claimant did not confine its business to making loans to members, nor to loans to nonmembers in times of small demand for member loans, nor to borrowing moneys (deposits) from nonmembers for the purpose of making loans to members, but, regardless of the borrowing needs of its members, accepted large deposits from nonmembers for the purpose of realizing profits from nonmember loans, from deposits in other building and loan associations and financial institutions, and from investments in mortgages

and other securities purchased from non-members.

And in the Motion for New Trial (pp. 8 and 9 thereof) the Government again urged this matter, as follows:

> The evidence in the case at bar shows that plaintiff did not confine its business to making loans to members during any of the years 1918 to 1923, inclusive (Stipulation of Facts, Exhibit No. 3); that it borrowed large sums from nonmembers (deposits) with no reference to and regardless of the borrowing needs of its members (Stipulation of Facts, Exhibit No. 4).

The witness Deselm (secretary of Respondent) (R. p. 42) testified:

> 503. Question. Now, during your connection with the association, were deposits ever refused from nonmembers?
>
> Answer. I don't remember that they were.
>
> 504. Question. So that regardless of the borrowing needs of your members, you still continued to accept deposits from non-members?
>
> Mr. Hamby. I object to that question. His receiving deposits from nonmembers has no relation to making loans to members, but enables the association to make loans.
>
> Mr. Horton. That is all right; just answer the question.
>
> The Witness. What is the question?
>
> Mr. Hamby. Read the question to him.
>
> (Question 504 read.)

The WITNESS. Certainly; not knowing what our borrowing needs would be from day to day until the applications were made.

505. Question. But you do know what the borrowing needs of your members were?

Answer. We would not know.

506. Question. You knew what loans you were making to your members?

Answer. Yes, sir.

III

THE RESPONDENT WAS NOT CONCERNED WITH THE PURPOSE OF THE BORROWER AND DID NOT LIMIT ITS LOANS TO THOSE TO BE USED FOR BUILDING OR OTHERWISE ACQUIRING HOMES. IT ACCEPTED AS SECURITY FOR MEMBER AND NONMEMBER LOANS MORTGAGES ON HOMES, REAL ESTATE, FARMS, BUSINESS PROPERTIES, CHURCHES, AND APARTMENT HOUSES, AS WELL AS BANK STOCK, INDUSTRIAL STOCK, MUNICIPAL BONDS, AND OTHER BONDS

While the findings of fact made by the Court of Claims in the Statement of Assets and Liabilities show loans on other securities than mortgage security (Item 4 of Assets, Finding VII, R. 9), and further show (Finding VIII, R. 10) that loans were made upon all of the kinds of property enumerated in this requested finding, and therefore the truth and accuracy of the requested finding can not well be questioned, it is believed a finding of the ultimate fact of the disregard of the purpose and method of operation of a true building and loan association is material to a proper determination of this case and should be made a part of the finding

by the court below. This matter was all requested by the Government in its Request No. III for Findings of Fact before the Court of Claims.

IV

RESPONDENT'S LOANS WERE NOT CONFINED TO BORROWERS WHO SUBSCRIBED TO STOCK EQUAL TO THE FACE OF THE LOAN, BUT IT PERMITTED PERSONS TO BECOME MEMBERS UPON SUBSCRIBING TO A NOMINAL AMOUNT OF STOCK (FROM ONE TO FIVE SHARES), REGARDLESS OF THE AMOUNT SOUGHT TO BE BORROWED. RETROACTIVE NOMINAL STOCK SUBSCRIPTIONS WERE RECEIVED BY RESPONDENT, AND IN CERTAIN CASES CREDITS OF THE BORROWER WERE APPLIED BY RESPONDENT TO NOMINAL STOCK WHERE NO STOCK SUBSCRIPTIONS HAD BEEN MADE BY THE BORROWER

These facts have a most important bearing upon the Government's theory of this case. Under the 1918 Act, and especially under the 1921 Act, which contains the specific provision that substantially all of the business of the company should be confined to the making of loans to members, the percentage of business with members and the percentage with nonmembers are very important points in determining the question of respondent's right to tax exemption. And where respondent departs from the plan of a true building and loan association, which requires the shares of a borrower to equal the amount of his loan, and permits not only nominal stock subscriptions but retroactive nominal stock subscriptions, and for the purpose testified by the Secretary of the respondent:

> Question. Because you conceived that would reduce your tax liability?
>
> Answer. Yes, sir (p. 55 of the record before the Court of Claims)—

it is submitted that such facts should be in the record which this Court has before it in determining the right of respondent to such exemptions.

This matter also becomes very important as it renders misleading, to the Government's prejudice, several of the facts which were found by the Court of Claims. For instance, the court purports in Finding VIII (R. 10), to set forth a tabulation of the loans to members and nonmembers, and in such table nominal stock subscribers, as well as retroactive nominal stock subscribers, are considered as members. If these persons were considered as members and their loans considered as loans to members, only to the amount of their stock, the percentages for the latter years during which respondent engaged in this practice of nominal stock subscriptions would show a much higher percentage of business with nonmembers. The Government requested findings upon this matter in its Request No. IV and renewed that request in its motion for a new trial (p. 11 thereof), quoting in support thereof the undisputed testimony of respondent's secretary, which has heretofore been set out in connection with the discussion of Item I hereof.

V

THE NUMBER OF DEPOSITORS IN EVERY YEAR EXCEEDED THE NUMBER OF STOCKHOLDERS, THE DIFFERENCE BEING SMALL IN 1918 BUT THEREAFTER THE NUMBER OF DEPOSITORS BEING APPROXIMATELY TWICE AS GREAT AS THE NUMBER OF MEMBERS IN EACH YEAR EXCEPT 1923, WHEN IT WAS MORE THAN THREE TIMES AS GREAT

This also tends to show the true method of operation and the nature of the business being conducted by respondent, indicating clearly not only that it had departed from the business of a true building and loan association and begun that conducted by a bank, but also that its business was not substantially confined to making loans to its members. There can be no question as to the accuracy of the finding requested, since it was the subject of a stipulation of facts between the parties. The following table and statement, as pointed out in the Government's Motion for a New Trial (p. 9 thereof), shows the correctness and materiality of this request in the Motion to Remand:

> The number of stockholders and number of depositors at December 31st of the respective years were as follows (Stipulation of Facts Exhibit No. 2):

	1918	1919	1920	1921	1922	1923
Stockholders	1,270	1,600	1,940	1,900	1,172	991
Depositors	1,570	1,922	2,080	2,200	2,410	3,025

Plaintiff's nonmember business, we submit, was disproportionate to its member

business during the calendar years 1918–1919 and 1920, as shown by Stipulation of Facts Exhibit No. 3, and certainly during the calendar years 1921, 1922, and 1923, substantially all of plaintiff's business was not done with members as shown by the same Exhibit No. 3.

CONCLUSION

For the reasons heretofore set out it is respectfully submitted that the Government's Motion to Remand for Additional Findings of Fact should be granted.

Respectfully submitted.

WILLIAM D. MITCHELL,
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HERMAN J. GALLOWAY,
Assistant Attorney General.
T. H. LEWIS,
Attorney, Bureau of Internal Revenue.

SEPTEMBER, 1928.